

SENATE FINANCE COMMITTEE  
February 2, 2021  
9:01 a.m.

[9:01:52 AM](#)

CALL TO ORDER

Co-Chair Stedman called the Senate Finance Committee meeting to order at 9:01 a.m.

MEMBERS PRESENT

Senator Bert Stedman, Co-Chair  
Senator Lyman Hoffman  
Senator Donny Olson (via teleconference)  
Senator Natasha von Imhof  
Senator Bill Wielechowski  
Senator David Wilson

MEMBERS ABSENT

Senator Click Bishop, Co-Chair

PRESENT VIA TELECONFERENCE

Deven Mitchell, Department of Revenue, Debt Manager, Juneau; Mike Barnhill, Department of Revenue, Deputy Commissioner, Juneau; Pam Leary, Department of Revenue, Treasury Director, Juneau.

SUMMARY

STATE DEBT SUMMARY

SAVINGS ACCOUNTS and CASH FLOWS

^STATE DEBT SUMMARY

[9:04:37 AM](#)

DEVEN MITCHELL, DEPARTMENT OF REVENUE, DEBT MANAGER, JUNEAU (via teleconference), presented, "January 2021 Credit Review and State Debt Summary" (copy on file). He pointed to slide 2, "State of Alaska and Other 49 States' Ratings."

Co-Chair Stedman asked that the slide be put into rating order from highest rating to lowest rating. He also requested the dates of each rating downgrade.

9:07:36 AM

Mr. Mitchell looked at slide 3, "Rating Challenges in 2021":

#### Political Challenge

- Failure to resolve the ongoing structural deficit during the 2021 Legislative Session will likely result in additional State credit downgrades
- Oil price declines have reduced state revenues and created significant fiscal imbalance since 2015
- Constitutional Budget Reserve Fund (CBR) allowed difficult decisions to be deferred over the last five years, this is no longer an option
- Reductions to general fund spending while significant, have been difficult to achieve and haven't eliminated the ongoing structural deficit
- Gridlock over use of Permanent Fund earnings Permanent Fund Dividend vs. public services

#### Financial Policies

- Structured 5 percent Percent of Market Value (POMV) draw insufficient to fully fund the budget and the dividend
- Statutory conflict between POMV draw and PFD formula
- Lack of consensus on long term options for either spending less money or generating more revenue

#### Rating Agency Concerns

- Ongoing structural UGF imbalance and reliance on near depleted one time financial resources (CBRF)
- Comparatively large net pension liability
- Narrow economy that is relatively small
- Perception that the State's economy and operating revenues are primarily reliant on petroleum development

9:12:29 AM

Senator von Imhof noted that there were only three states that had a worse credit rating than Alaska. She remarked that the governor's proposal had a \$350 million GO bond proposal, but the revenue generated by the state would be used to pay the dividend. She queried the details of the examination by the rating agency.

Mr. Mitchell replied that the state's ability to sell GO bonds was going to be in place whether there was a solution to the fiscal situation or not.

9:15:40 AM

Senator Hoffman queried the estimated rating from Mr. Mitchell's perspective. He recalled that the year prior had a \$680 dividend, but the governor was proposing three times that number. He noted that there was a chart prepared by the Legislative Finance Division (LFD), which would be the largest appropriation at 32 percent of the budget. He stated that it would overdraw the 5 percent by something larger than 10 percent. He queried any remarks on that drastic move and its affect on the rating.

Mr. Mitchell responded that the impact of Covid 19 was recognized in all aspects, so there was some mitigation for overdrawing of the reserves for the purpose of stimulating the economy through dividend distribution. He stated that an overdrawing of the Earnings Reserve Account (ERA) would not be seen favorably by rating analysts. He stated that the analysts worked with other agencies that had endowments, like universities, and there were guidelines for reasonable withdrawals of the funds. He stated that there could be an impact on the rating.

Senator Wielechowski queried the debt cost of the additional downgrade to the state's rating.

Mr. Mitchell responded that the percentages would be nominal. The cost of capital vs the downgrade may only result in a small decrease.

Co-Chair Stedman asked about downgrades.

Mr. Mitchell stated that it was different from a mortgage - there was a rate for every year of the loan. Once the maturities were sold, they did not adjust for credit ratings.

[9:21:17 AM](#)

Senator Wilson asked about the strength of the Alaska Permanent Fund Corporation (APFC) overall. He felt that the strength of APFC should or could result in a more positive rating.

Mr. Mitchell agreed, and recalled a presentation from the year prior which showed that the state had been working to further educate the analysts the strength of the APFC. He noted that the majority of UGF was coming from a sovereign wealth fund, so there was not a reliance on the state's economy. He noted that focusing on the state's economy was a faulty analysis, because of the more than 3000 investments that were making throughout the world.

Senator von Imhof shared calculations based on the percentages.

Senator Wielechowski queried the efforts to get the message out about the credit rating. He noted that the next presentation had a number of days that each state could run on total balances. He remarked that Alaska had the largest savings account in the country, by far at over 170 days. He wondered whether there could be greater effort to get the message out that Alaska was in good financial shape.

Co-Chair Stedman felt that the question was better for the upcoming presentation. He requested that the answer be brief.

Mr. Mitchell stressed that those points were made in every ratings presentation. He agreed to provide those discussions.

[9:27:48 AM](#)

Mr. Mitchell presented slide 4, "Alaska's Most Pressing Credit Rating Challenge":

- The CBRF receives additional dispute resolution deposits and restricted earnings

- Post FY2019, it was determined that adjustments to the CBRF account balance was necessary for dispute resolution deposits originally deposited to the General Fund
- The Governor's budget has proposed drawing just \$39.6 million from the CBRF for FY2022

[9:33:23 AM](#)

Co-Chair Stedman requested another POMV column be added to the slide to clarify the delineation. He wondered whether there should be a clarification about total revenues versus total expenditures.

Mr. Mitchell replied in the affirmative, and shared that the net position would be all revenue not only unrestricted revenue.

Senator von Imhof believed that there were previous presentations that showed that the governor's deficit was larger than \$39 million, but rather over \$1 billion. She queried the location of the funds to cover the deficit.

Mr. Mitchell replied that the \$39 million draw on the CBR was prior to the Permanent Fund Dividend (PFD) distribution. Therefore, any distribution of dividends would result in a higher deficit. He added that the only source to fund the PFD was the ERA.

[9:35:44 AM](#)

Senator von Imhof surmised that an ad hoc draw from the ERA would result in a greater amount than the 5 percent allotted for the POMV. She wondered how the draw of greater than 5 percent would affect the state's ratings.

Mr. Mitchell replied that it would "run afoul" from a ratings perspective for the use of an endowment. He stated that it could make sense, however, from a policy perspective.

Mr. Mitchell looked at slide 6, "State Debt Obligation Process":

All Forms of State Debt are Authorized First by law

- May be a one-time issuance amount or a not to exceed issuance limit in statute
- General obligation bonds must then also be approved by a majority of voters
  - General obligation bonds are the only debt secured by full faith credit and taxing authority

All State Debt must be structured and authorized by the State Bond Committee

- Includes general obligation bonds, subject to appropriation issues, and state revenue bonds

The State Bond Committee determines method and timing of debt issues to best utilize the state's credit and debt capacity while meeting the authorized project's cash flow needs

The State has established other debt obligations

- Reimbursement Programs

The School Debt Reimbursement Program or HB 528 reimbursement

Not currently authorized for new debt and periodically funded (was most recently partially funded in 2017 and 2020, no appropriation in the FY2021 Budget)

- Retirement Systems

Unfunded actuarially assumed liability (UAAL) for defined benefit employees is guaranteed by the Constitution

Annual payments on the UAAL of other employers is reflected as State debt in the CAFR

Some flexibility in how payments are made

[9:41:31 AM](#)

Co-Chair Stedman felt that there should be a focus on the pertinent working issues in the committee.

Mr. Mitchell highlighted slide 7, "Total Debt in Alaska at June 30, 2020." He shared that the table was from the state's debt book. He ran through the details of the slide.

Mr. Mitchell pointed to slide 8, "Total Debt in Alaska at June 30, 2020." He remarked that the University was listed under Revenue Bonds, and further detailed the information on the slide.

[9:46:37 AM](#)

Senator Hoffman wondered whether the 2 percent refinancing interest rates was a possibility, and queried the administration's position.

Mr. Mitchell responded that the administration was paying attention to the low interest rates. He explained, however, that there was a difficulty in refinancing bonds in advance of the call date. He shared that, when municipal bonds were sold, they were almost always sold with a ten-year hard call. He explained that those bonds could not be refinanced for the first ten years, and only bonds that were mature after the first ten years could be eligible for refinancing.

Senator Wilson wondered whether there had been full repayment of the \$39 million for Alaska Industrial Development and Export Authority (AIDEA) Revolving Loan Fund, because he did not see it included in the list.

Mr. Mitchell agreed to provide that information.

[9:49:54 AM](#)

Mr. Mitchell looked at slide 9, "Current General Fund Annual Payment Obligation":

GF Payment peaked in 2018 at \$225.2 million

Declining payment in every year (50 percent of peak in

PERS/TRS special funding payments grow, but less dramatically

PERS TRS special funding is many times all other state commitments

Senator von Imhof asked for a restatement of the graphic in the slide with an overlay of the GO Bond.

Mr. Mitchell agreed to provide that information.

Mr. Mitchell highlighted slide 10, "UGF Budget Impact":

UGF Budget Impact of \$350M GO and \$100M AHFC Revenue  
Bond Proposals Bond

GO BOND

- Full Faith and credit of SOA
- Requires Legislative and Voter approval
- First bond issuance likely in FY 2023

Revenue Bond

- Debt service is paid via revenues generated

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Co-Chair Stedman remarked that there would be additional detail about the slide when the committee considered the capital budget. He requested a debt service schedule.

Mr. Mitchell looked at slide 11, "Limited State Short Term Debt Obligation Alternatives":

Bond Anticipation Notes (AS 37.15.300 390)

- May be used when long term debt is authorized by law
- While short term, it is expected to be a precursor of long term debt
- May be used to avoid negative carry in construction funds, better match long lived projects and their financing, or as an additional budget management tool
- Directly impacts long term debt affordability

Revenue Anticipation Notes (AS 43.08.010)

- May borrow money when it becomes necessary in order to meet appropriations for any fiscal year in anticipation of the collection of the revenues for that year
- All notes and interest thereon shall be paid from revenue by the end of the fiscal year next succeeding the year in which the notes were issued
- May be tax exempt if a bona fide revenue deficit occurs during the fiscal year

Earnings of the Permanent Fund and other available fund earnings, will need to be included in determining if a revenue deficit occurs

- The State has not used since the late 1960's



10:00:23 AM

Mr. Mitchell addressed slide 13, "Debt Affordability Analysis":

Annual analysis required by AS 37.07.045 to be delivered by January 31

Discusses credit ratings, current debt levels, history and projections

Relies upon debt ratios, limit of 4 percent for directly paid state debt, and 7 percent when combined with municipal debt that the state supports

-Beginning in FY 2019 UGF revenue increased significantly due to reclassification of certain Permanent Fund earnings. Uncertainty about this revenue in future years warranted reductions of 1 percent to debt ratios.

Identifies currently authorized, but unissued debt

Establishes refinancing parameters

Determines a long term debt capacity at current rating level

Discusses, but doesn't define a capacity for short term debt

Does not include State Agency GO or Revenue Bonds, or SOA Revenue Bonds

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Mr. Mitchell pointed to slide 14, "Authorized Bonding Authority":

- The State had no authorized but unissued general fund obligations (post GO Series 2020A issuance)
- As of June 30, 2020, the State had debt obligations secured and paid by the general fund of approximately \$727.3 million
  - \$624.9 million of general obligation bonds,

- \$20.6 million of Certificates of Participation, and

- \$182.6 million of lease revenue bond conduit issues of political subdivisions.

- The 2020 A general obligation bonds closed on August 5, 2020 in the amount of \$84.56 million to generate \$110.3 million of project funding.

- The 2020 A bonds annual debt service is approximately \$7 million per year.

Co-Chair Stedman wondered whether there had been issuance of all authorizations.

Mr. Mitchell replied in the affirmative.

Co-Chair Stedman queried any concerns about being timed out of the IRS rules about usage of the money.

Mr. Mitchell replied that he did not believe so.

Co-Chair Stedman requested that answers be more succinct.

[10:05:23 AM](#)

Mr. Mitchell looked at slide 15, "January 2021 Debt Affordability Analysis." He explained that there was an estimated capacity for the state at \$1 billion with the caveat the state might be downgraded anyway. He shared that there was a belief that the state would not be downgraded to the level without progress on a fiscal plan as a result of the issuance of up to \$1 billion as part of a ten-year capital program. He pointed out the details of the slide.

Mr. Mitchell pointed to slide 16, "Authorized but Unissued State Debt":

Currently there is no authorized but unissued direct State debt (paid from the General Fund):

The final \$110,348,242 in authorized GO bond funding was issued on August 5, 2020. This was the final tranche of funding for the 2012 Transportation Bond Act. There is no remaining GO bond issuance authority at this time.

The authorized \$300 million Knik Arm Crossing State supported bond structure was invalidated by the September 4, 2020 decision of the Alaska Supreme Court.

The authorized \$1 billion Alaska Tax Credit Certificate Bond Corporation State supported bond structure was invalidated by the September 4, 2020 decision of the Alaska Supreme Court.

The authorized \$1.5 billion Alaska Pension Obligation Bond Corporation State supported bond structure was invalidated by the September 4, 2020 decision of the Alaska Supreme Court.

While not State debt, the school debt reimbursement program is not currently authorized.

Co-Chair Stedman surmised that all of the bond authorizations were now moot.

Mr. Mitchell replied in the affirmative.

Senator von Imhof wondered whether there should be a discussion about the Alaska Railroad Bond debt.

Mr. Mitchell replied that he did not believe that had been invalidated, and stated that the upcoming slides would address that question.

[10:09:54 AM](#)

Mr. Mitchell highlighted slide 18, "State Supported Debt Structure ATCCBC." He explained that the structure had the state committing to pay a sub-entity of the state on a subject-to-appropriation basis.

Mr. Mitchell discussed slide 17, "ATCCBC and Other Subject to Appropriation Debt":

- The Alaska Tax Credit Certificate Bond Corporation ('ATCCBC') was created to re finance up to \$1 billion of oil and gas tax credits using a state subject to appropriation credit pledge bond structure, but with

statutes that also allowed a state moral obligation pledge even though it wouldn't likely be used.

- On September 4, 2020, the Alaska Supreme Court issued a decision that disallowed the structure contemplated for the Alaska Tax Credit Certificate Bond Corporation and placed additional limitations on when the State can issue State Supported debt

- The decision reaffirmed the Carr Gottstein Supreme Court decision allowing for lease purchase of real property arrangements like certificates of participation or lease revenue bonds.

- The expected ATCCBC structure involved the ATCCBC entering a contract with the State of Alaska, Department of Revenue to provide funds for the purchase of the discounted credits in exchange for future payments (subject to appropriation). The funds provided would be bond proceeds and the future payments would be equal to ATCCBC's bonds' debt payments which would be subject to annual appropriation.

- Due to similarity of structure it is clear that the decision also rendered the Pension Obligation Bond Corporation, and the Toll Bridge Revenue Bonds for the Knik Arm Bridge, illegal

- The inclusion of the moral obligation construct in the ATCCBC's statutory structure resulted in certain broad references in the decision which may impact other bond programs with constructs that while fundamentally different from the ATCCBC in both public purpose and bond structure use moral obligation debt.

- On September 28, 2020, the State of Alaska Department of Law filed a Petition for Rehearing with the Supreme Court in an attempt to obtain clarity on the scope of the Court's intent in their decision

- The Court has not yet responded to the Petition for Rehearing

Mr. Mitchell pointed to slide 19, "Moral Obligation Structure Alaska Municipal Bond Bank." He pointed to the pertinent information within the slide.

^SAVINGS ACCOUNTS and CASH FLOWS

[10:15:33 AM](#)

MIKE BARNHILL, DEPARTMENT OF REVENUE, DEPUTY COMMISSIONER, JUNEAU (via teleconference), introduced himself.

PAM LEARY, DEPARTMENT OF REVENUE, TREASURY DIRECTOR, JUNEAU (via teleconference), discussed, "State of Alaska; Update on the State's Cash Reserve Funds and Discussion of State Cash Flows." She looked at slide 2, "Agenda":

1. Update on Cash Reserve and Other Funds
2. State Cash Flows
3. Revenue Volatility Management

Ms. Leary pointed to slide 4, "FY22 Days that Alaska could run on Total Balances (Cash Reserve and Other Funds)." She stated that the slide showed the number of days that "Alaska could run" on the total balances without revenue.

Senator Wielechowski wondered whether there was a belief that AIDEA could be used when there was an exhaustion of the CBR.

Ms. Leary deferred to Mr. Barnhill.

Mr. Barnhill replied in the affirmative.

Senator Wielechowski asked why AIDEA was not included in the slide.

Ms. Leary replied that it was not included because the slide showed funds that could be turned to by the legislature in "fairly short order." She agreed to update the slide to include AIDEA funds.

Senator Wilson asked whether the use of those funds would cripple AIDEA's ability to bond.

Mr. Barnhill responded that the use of AIDEA funds for non-AIDEA purposes had negatively impacted their bond rating in the past, so the use of those funds would likely affect their rating in the future.

Co-Chair Stedman asked whether that explanation had address Senator Wielechowski's question.

Senator Wielechowski replied that it adequately addressed his question for the time being.

10:20:16 AM

Ms. Leary addressed slide 5, "Days Each State Could Run on Total Balances in FY 2019." She felt that the 2020 comparison would look somewhat different from the representation on the slide. She noted that, even with large draws, Alaska was second only to Wyoming in terms of days that the state could run. She noted that the median of each state was up from 40.4 days in 2018 to 49.7 days in 2019.

Co-Chair Stedman wondered whether of the other states had a similar endowment to Alaska, relative to the size of the state such as the ERA.

Ms. Leary replied that Wyoming had a similar type of sovereign fund. She added that there were other smaller sovereign endowments that were in some of the other states, such as Texas and New Mexico.

Senator Wielechowski felt that the 178 days that Alaska could function figured approximately \$11 million a day. He remarked that it would total \$2 billion in assets. He queried the accuracy of that calculation.

Ms. Leary replied that the amount was based on a survey of all states. She felt that number was based on the accessibility of funds in the CBR.

Co-Chair Stedman requested the data of the slide's basis.

Ms. Leary looked at slide 6, "Cash Reserve Comparisons to Other States":

Although uneven across states, since the Great Recession, states have increased cash reserve funds with a median balance of 7.9 percent in 2019 from 4.8 percent in 2008. Enacted FY21 percentages targeted an even higher median percentage of 8.4 percent prior to COVID 19.

Ms. Leary highlighted slide 7, "Cash Reserve Considerations":

Cash reserves range from 2 percent to 20 percent of General Fund Expenditures and should reflect the risk volatility of the revenue stream

According to the PEW Trust, the optimal savings target of a state depends on three factors:

The defined purpose of funds (cash flow, revenue shortfall, combination)

The volatility of a state's tax revenue

The level of coverage similar to an insurance policy that the state seeks to provide for its budget (how likely is a 10 percent vs. a 50 percent revenue decline).

All but eight states cap the balance of their fund. The cap is typically based on total general fund revenues (ranging from a cap of 2.5 percent to 15 percent) or total general fund appropriations (ranging from a cap of 2 percent to 20 percent).

There is a trade off that needs to be considered in determining the prudent balance of the fund.

State Revenue since POMV implementation has been as high as \$5.3B (2019) and as low as \$4.2B (2020)

Co-Chair Stedman felt that the reserve number would be a focus, so Ms. Leary should take that into consideration.

Ms. Leary looked at slide 8, "Constitutional Budget Reserve Fund (CBRF) Historical Invested Assets (in billions)":

Data is at fiscal year end of June 30.

In 1990, voters of Alaska adopted an amendment to the constitution creating the CBRF.

CBRF is used to fund temporary cash flow expense/revenue mismatches.

CBRF is used to appropriate/cover budget revenue shortfalls.

Appropriations from the CBRF must be repaid.

Co-Chair Stedman wondered why the Statutory Budget Reserve (SBR) was not included in the chart.

Ms. Leary replied that the SBR was a part of the general fund, and was broken out into portions. She stated that the SBR was managed separately for a short period of time, but was then moved back into the management of the general fund.

10:30:20 AM

Co-Chair Stedman requested that the delineation of the SBR as a subcomponent of the general fund be incorporated into the slide.

Ms. Leary agreed to provide that information.

Mr. Barnhill shared that the SBR was depicted on slide 14.

Senator von Imhof queried the consequences of not paying back the CBR.

Co-Chair Stedman requested the timeframe of the amortization of the debt.

Mr. Barnhill explained that it reflected the constitutional requirement for repayment of the CBR. He stressed that there was no time period or interest rate.

Ms. Leary discussed slide 9, "Constitutional Budget Reserve Fund Fiduciary oversight: Commissioner of Revenue." She stated that the slide showed some investment statistics on the CBR.

Ms. Leary addressed slide 10, "Power Cost Equalization (PCE) Historical Invested Assets (in millions)":

The purpose of the PCE Endowment fund is to provide for a long term stable financing source that provides affordable levels of electric utility costs in otherwise high cost service areas of the state.

5 percent of the monthly average market value of the fund for the previous 3 fiscal years may be appropriated. If prior years earnings exceed this amount, 70 percent (not to exceed \$55M) of the difference can be spent on related identified programs.



Ms. Leary highlighted slide 11, "Power Cost Equalization Fund Fiduciary oversight: Commissioner of Revenue." She noted the 50 percent equity and 40 percent fixed income target asset allocation. She noted the projected ten-year return of 5 percent, and the one-year rolling average.

Senator Wilson wondered why the PCE fund had been flat since 2018. He also asked why the projection had been reduced from the year prior.

10:35:38 AM

Ms. Leary replied that since 2016 the fund had been increasing, because of the returns and the growth rate, which were just slightly above the appropriations. She shared that the target date returns were developed with the team with the commissioner's approval. She stated that in the recent year, there was a slight change in the allocation and the target of each asset classes.

Co-Chair Stedman remarked that the funds would be detailed later in the legislative session.

Ms. Leary pointed to slide 12, "Alaska Higher Education Investment Fund (AHEIF) Historical Invested Assets (in millions)":

On September 1, 2012, the AHEIF was capitalized with a \$400 million deposit from receipts of the Alaska Housing Capital Corporation for use in paying Alaska Performance Scholarship Awards and AlaskAdvantage Education Grants.

Ms. Leary looked at slide 13, "Alaska Higher Education Investment Fund Fiduciary oversight: Commissioner of Revenue." She noted that the fund had a high risk tolerance.

Co-Chair Stedman queried the definition of "high risk."

Ms. Leary agreed to provide that information, and explained that there was a range within the definition of "high risk."

Co-Chair Stedman remarked that there was a significant allocation difference.

10:40:37 AM

Ms. Leary pointed to slide 14, "General Fund and Other Non-Segregated Investments (GeFONSI) Historical Invested Assets (in billions):

GeFONSI includes the General Fund and Other Non segregated funds invested in a pool environment (GF proper= \$400 million).

GeFONSI II was created in 2018 to target a higher risk return profile for a subset of funds.

Co-Chair Stedman requested a chart with the SBR included with the CBR. He remarked that there were different views in the committee related to those accounts as savings mechanisms. He noted that in 2012, GeFONSI had \$9 billion, and was now currently at \$3.5 billion. He remarked that the SBR had been liquidated from \$2.6 billion to zero. He asked about the magnitude of decline in GeFONSI.

Ms. Leary replied that there was a combination of factors that resulted in the difference. She stressed that some of the funds in GeFONSI had higher balances, and had since been managed to a lower amount. She stated that there was not as "strict an eye" in maintaining the money in the operating account. She stated that the management had since been more structural to maintain in terms of calling cash to the operating fund for payment day to day expenses. She pointed out that the slide included the Higher Education Fund, so there was approximately \$400 million since its inception. She remarked that the number was actually currently \$2.5 billion.

Co-Chair Stedman wondered where the funds were distributed.

Ms. Leary replied that the funds were spent, and there was not as rigorous an effort to maintain a lower balance in the general fund. She agreed to provide a comparison of the funds.

10:45:27 AM

Co-Chair Stedman remarked that he was concerned about the "burn rate of cash." He queried the actual burn rate of the funds.

Senator von Imhof remarked that there was a cost shift between undesignated to designated general funds (UGF and DGF). She remarked that there could appear to be an elimination of programs, but the fund source had a shift.

Co-Chair Stedman stated that work was done on that subject.

Ms. Leary presented slide 15, "General Fund and other non-segregated investments (GeFONSI I and II) Fiduciary oversight: Commissioner of Revenue." She noted that the combined total was \$2.5 billion.

Senator von Imhof feared that the Callan projection was too high when there was a point of the low rate. She did not believe that there would be a significant return on the investment.

[10:49:50 AM](#)

Ms. Leary pointed to slide 16, "Public School Trust Fund (PSTF) Historical Invested Assets (in millions)":

The PSTF was established in 1978, replacing the territorial era public school land grant originally created by congress in 1915, by a transfer of the balance from the permanent school trust.

Following passage of HB 213 in 2018, the fund is now managed as one fund, under a percentage of market value method (5 percent of the average market value for the 5 years preceding the last previous fiscal year).

Ms. Leary highlighted slide 17, "Public School Trust Fund, Fiduciary oversight: Commissioner of Revenue." She remarked that the slide showed a slightly higher risk. The target allocation included a target of equity to fixed income.

Co-Chair Stedman requested a slide that showed the allocation to the fixed income with the same risk allocation.

Ms. Leary agreed to provide that information.

Senator von Imhof recalled that there was a bill passed the previous year about the lottery for the Public School Trust Fund. She asked if any of the money would go to that fund.

Ms. Leary replied that it was purely the earnings of fund offsetting the appropriation. She noted that there were separate funds set aside for the lottery.

Mr. Barnhill added that the state funds were invested by the DOR commissioner. He remarked that there had been some advice to add a layer of governance, and he pointed out that there had been governance applied to those funds since that request.

Co-Chair Stedman assumed the governance was used for not only Public Employees' Retirement System (PERS) and Teacher Retirement System (TRS), but also to assist the DOR commissioner in other decisions.

Mr. Barnhill replied that the governance would advise the commissioner with respect to the investment of the state funds.

Co-Chair Stedman felt the governance would help the commissioner to make better decisions. He understood that decisions might not be the most profitable in hindsight, but the commissioner could show a rationale to the decision.

Mr. Barnhill agreed.

[10:56:01 AM](#)

Ms. Leary addressed slide 18, " Public Employees Retirement System and Teachers Retirement System (PRS and TRS) Pension and Health Defined Benefit Plans Historical Invested Assets (in billions0":

The Alaska Retirement Management Board (ARMB) is a 9 person board that is the fiduciary of the state's pension and health systems.

The defined benefit plans currently experiences net outflows from the funds.

The 36 year return Average for PRS/TRS was 8.91 percent.

Ms. Leary pointed to slide 19, "Public Employees Retirement System and Teachers Retirement System, Fiduciary oversight: Alaska Retirement Management Board."

Senator Wielechowski requested a similar pie chart for the AIDEA account.

Co-Chair Stedman agreed, and would acquire that information.

Mr. Barnhill replied the Treasury Division did not manage the AIDEA funds, but would reach out to provide that information.

Co-Chair Stedman stated that the information would be helpful if it were correlated together in the presentation.

[11:00:02 AM](#)

Ms. Leary looked at slide 21, "Cash vs. Accrual balances":

Cash balance is what you have in the bank at a given point in time.

Accrual balance is what you have earned and what liabilities have been incurred at a particular point in time. It is what you should have at a particular point in time after all expected receipts and expenditures come in and out.

Treasury fund balances are cash balances, not what is available to spend.

Ms. Leary discussed slide 22, "SOA Treasury Cash Flow":

Cash Inflows

- Tax Revenues
  - Oil and Gas, Excise, Other
- Federal Dollars
  - Grants, Medicaid, FHWA, Education, Other
- Earnings Reserve Funds
- Agency Receipts
  - Fees, Licenses, Permits, Fines, Other

Cash Outflows

- School Education Payments
- Payroll and Pension Payments

- Vendor Payments
- Medicaid Payments
- External Program Grant Payments
- Debt Service Payments Cash Outflows

Senator Wielechowski recalled testimony about corporate income tax payments, and queried the source of that money.

Ms. Leary replied that the money would come from the general fund.

Senator Wielechowski wondered whether that payment required a legislative appropriation.

Mr. Barnhill replied that it did not require an appropriation, but was a reversal of the payment to the general fund.

Ms. Leary highlighted slide 23, "Cash Flow Deficiencies":

Prior to 1985, most unrestricted revenues flowed into and stayed in the General Fund for expenditure.

Over time, the legislature has established many subfunds to segregate cash for budgeting purposes, resulting in less cash available to pay day to day operating costs.

Expenditures can occur prior to receipt of revenue, resulting in cash flow timing mismatches:

Federal programs require expenditures before reimbursement.

i.e. Medicaid, Transportation, etc.

Beginning of year appropriation transfers do not match incoming revenue.

i.e. State pension payments, transfers to sub funds

Seasonal Cash Flow needs.

i.e. Summer is the peak season for construction projects and seasonal workers.

[11:06:49 AM](#)

Senator Wielechowski wondered whether the corporations would be receiving the same net operating loss refunds on both the state and federal taxes.

Mr. Barnhill replied that they did not have a line of sight on federal income tax impacts, but agreed to provide further information.

Senator Wielechowski was not convinced that the payments did not require legislative appropriation. He did not believe that it was a simple accounting issue.

Co-Chair Stedman remarked that the issue would be worked through for clarity.

Senator Wielechowski recalled that the department was aware of the issue in the previous May, and wondered why no action had been taken to fix the situation.

Co-Chair Stedman asked that the department address the timeline of the approach to the issue.

Mr. Barnhill stated that the payment system had not changed since he had been with the department.

[11:10:18 AM](#)

Ms. Leary pointed to slide 24, "Cash Deficiency Memorandum of Understanding":

Developed in 1994 between DOR, DOA, OMB and LAW.

Updated as needed.

Targets \$400m minimum cash threshold in the General Fund proper.

Outlines procedures for addressing cash flow timing mismatches:

Develop monthly cash projections.

Monitor daily general fund cash balances.

Perform temporary inter fund borrowing.

Transfer from SBR, CBR and ERA or sub funds.

In the event of revenue shortfall:

Seek legislative action through the Governor to access additional funds through appropriation from other Cash Reserve Funds discussed above.

Prioritize disbursements, restrict expenditures.

Senator von Imhof assumed that the update was between the legislature and DOR. She asked whether the department would submit a proposal of the updated memorandum of understanding (MOU).

Ms. Leary replied that the MOU was between the DOR, OMB, and LAW. She explained that it was updated as needed according to changes.

Senator von Imhof wondered whether the legislature would be involved in the process, or whether it was based on a threshold.

Mr. Barnhill replied that there was an attempt to draw a clear distinction between cash flow timing mismatches. The slide showed the expectation of revenue delivery.

Co-Chair Stedman hoped that the committee would have the information to anticipate the shortfall.

Ms. Leary commented on the MOU. She stated that the job was to forecast the cashflow, and she recalled a cap on the amount of borrowing that resulted in the department asking the legislature to mitigate the determination of which expenditures would get payment.

Ms. Leary looked at slide 25, "Cash Flow Deficiencies":

Use of budget reserve funds has been the solution of cash flow timing mismatches and revenue shortfalls.

Appropriations From Reserve funds

The Legislature includes language annually in the operating budget appropriating budget reserve funds for revenue shortfalls.



Treasury has relied on this appropriation to authorize use of budget reserve funds to address timing cash flow mismatches as well.

The CBRF was fully repaid by FY10.

Borrowing from the CBRF recommenced in FY14.

Per FY19 CAFR \$12.6B is owed to CBRF.

11:19:11 AM

Ms. Leary looked at slide 27, "Revenue Volatility has transitioned and now comes from":

#### Commodity Volatility

Petroleum revenues are 19 percent of FY22 projected unrestricted general fund revenues.

Uncertainty exists "in year" for FY22.

Will always have in year uncertainty because we base budget on in year oil collections.

#### Investment Return Volatility

Investment earnings are 72 percent of FY22 projected unrestricted general fund revenues.

Certainty exists today for FY22 (lagging POMV formula).

Uncertainty today for FY23 and beyond.

Mr. Barnhill furthered that through previous 2018 legislation, SB 26, the state had dramatically reduced its revenue volatility. He stated that there was some certainty for a fiscal year, and he thanked the committee for that bill.

Ms. Leary pointed to slide 28, "Volatility Management Techniques":

Access Cash Reserve and Other Funds (CBR and other fund balances).

Modernize fiscal tools to include lines of credit in addition to revenue anticipation notes.

Manage timing of Earnings Reserve Account transfers to the General Fund.

Manage timing of expenditures.

Senator von Imhof stressed that the money supported the economy, and people depended on that money.

11:24:00 AM

Ms. Leary highlighted slide 29, "Take Aways":

Declining cash reserves will continue to be a concern if budget deficits continue.

Even if the budget is balanced, and all revenue is received, cash flow timing mismatches will occur.

Cash flow forecasting is always wrong.

Revenue shortfalls may occur if forecasted assumptions are wrong.

Higher revenue volatility requires greater cash reserves until volatility decreases.

Volatility management techniques are available.

11:25:52 AM

Co-Chair Stedman wondered whether a redefining of structural deficit could be a solution.

Mr. Barnhill stated that, given the structural deficit the basic tools were new revenues, budget reductions, and changing the PFD formula.

Co-Chair Stedman recalled that there had been a presentation that showed future deficits couched as future revenues. He did not believe that defining it as revenue would be helpful for DOR to make its payments.

#  
ADJOURNMENT

11:28:07 AM

The meeting was adjourned at 11:28 a.m.